

SUBJECT: Licensing and rules for insurance advisory organizations

COMMITTEE: Insurance — favorable, without amendment

VOTE: 8 ayes — Smithee, Eiland, Burnam, J. Moreno, Olivo, Seaman, Thompson,
Wise

0 nays

1 absent — G. Lewis

WITNESSES: For — Howard Walker, Insurance Services Office, Inc.

Against — Birny Birnbaum

BACKGROUND: The Texas Insurance Code Art. 5.73 governs insurance advisory organizations. These organizations are private companies that sell statistical research data and forms to insurance companies. Under current law, Texas insurance companies may exchange with advisory organizations such information as:

- ! supplementary rating information;
- ! policy forms and endorsements;
- ! research and performance of inspections, except final rates or recommendations regarding profit or expense provisions, other than expenses related to losses; and
- ! prospective loss costs, except that a Texas insurance company may not receive prospective loss costs for personal automobile, homeowners', or dwelling fire insurance.

Prospective loss costs are estimates of the costs that an insurance company might be required to pay to cover policy-holders for different types of insurance.

Advisory organizations and insurance companies are prohibited from trading information on rate recommendations, profit, or expenses, other than expenses related to losses.

There is no license requirement for advisory organizations. However, several conditions must be met before an organization can share information with a Texas insurance company, including that it must have a subsidiary in Texas. Advisory organizations also must file with the commissioner a list of their Texas customers and the information or products purchased by each of those customers.

The commissioner may request from an advisory organization a summary of the actuarial assumptions, trend factors, economic factors, and other criteria used in trending data for Texas insurance companies.

Insurance companies that rely on prospective loss costs from advisory organizations must justify to the commissioner that they need the information due to insufficiency of their own data. Insurers that cannot justify their use of the information cannot file or use that information.

DIGEST: HB 2752 would create a license for insurance advisory organizations. Texas insurance companies would not be able to exchange information with an unlicensed advisory organization.

A licensed advisory organization could file prospective loss costs, supplementary rating information, and policy forms with the commissioner. These filings would be subject to the same rules applied to rate filings by insurance companies in that particular line of insurance. An insurance company that subscribed to an advisory organization could use this filed information and incorporate it into the company's rate filings.

HB 2752 would allow insurance companies and advisory organizations to exchange information on the actual rates of individual insurance companies. This would end the prohibition against exchange of such information.

HB 2752 would eliminate the requirement for insurance companies to justify their use of prospective loss costs from advisory organizations. Instead, the commissioner would review the rate filing of an insurance company that relied on prospective loss costs from an advisory organization. The commissioner also could require the insurance company to present its actual data and loss experience.

The bill would eliminate the requirement that an advisory organization has to have a subsidiary in Texas. To obtain a license, applicants would pay a \$100 fee. A corporation, unincorporated association, partnership, or individual would be able to apply for a license.

License applicants would specify the type of insurance information they would supply and file with the commissioner their constitution and bylaws, rules governing their activities, and a statement of their qualifications.

The commissioner of insurance would have to act on an application within 60 days. The application would remain in effect until the commissioner suspended or revoked it.

HB 2752 would take effect September 1, 1999. Existing insurance advisory organizations would continue to operate until their licenses were issued or denied.

**SUPPORTERS
SAY:**

HB 2752 would streamline the rules governing insurance advisory organizations. These organizations are crucial to the insurance industry, allowing companies to lower their overall costs by purchasing complex data and statistical information rather than having to generate it themselves.

Small insurance companies do not have enough claims and loss experience on their own to price their products efficiently without help from insurance advisory organizations. Companies entering new markets rely on insurance advisory organizations because they lack data on new markets.

An advisory organization license would work better than current requirements for advisory organizations in Texas. The Texas subsidiary requirement, in effect, has little meaning, since advisory organizations can establish token subsidiaries in Texas by holding one meeting of a meaningless subsidiary governing board.

Allowing advisory organizations to supply and receive actual insurance rates makes research and data collection easier. Insurance companies still would be required to determine their own rates and file them according to the Texas Insurance Code. There is no reason to exclude final rates from the information that an advisory organization can collect and distribute.

State regulation alleviates antitrust and monopoly concerns in the insurance industry. The commissioner could challenge any questionable rate filing.

HB 2752 would not decrease the regulatory authority of the insurance commissioner. Insurance companies and advisory organizations still would be responsible for their practices and could be kept out of the marketplace by the commissioner. Information filings by advisory organizations would be subject to the same rules applied to insurance rate filings and could be reviewed by the commissioner.

In current practice, the requirement that insurance companies must justify their use of advisory organization data in every case is just a technical hurdle without real regulatory involvement. HB 2752 would change the system to allow the commissioner to inspect the rate filing and advisory organization data of a particular insurance company rather than every one of them. The commissioner would be better able to isolate problems and remedy them without wasting resources on rubber-stamping every use of advisory organization data.

**OPPONENTS
SAY:**

Advisory organizations allow exactly the same type of collective rate-making that is prohibited by antitrust laws. The only reason that insurance companies are not subject to antitrust laws is because they are part of a regulated industry. However, regulatory requirements in Texas have gradually been decreasing. Thus, anti-trust protections and fire walls to protect against the exchange of rate information should be increased.

This bill would open the door to much more exchange of information on insurance rates through advisory organizations than has previously been allowed. Advisory organizations should be regulated even more closely because information from these organizations is used to determine nearly every insurance rate in Texas.

Under current law, advisory organizations and insurance companies are prohibited from trading information on actual rates. This prohibition is intended as an antitrust measure, working with other sections of the article to prevent price-fixing by insurance companies through advisory organizations. Yet HB 2752 would end this prohibition, which protects the insurance-buying public.

HB 2752 would not clearly require that the commissioner evaluate and authorize the information filed by these organizations. The information should be not used until the commissioner determines that the information is accurate. If information used for rate filings is not evaluated at the level of the advisory organization and the insurance company, there could be uncertainty in the market regarding the accuracy of the information.

If prospective loss costs supplied by an advisory organization are going to be used, insurance companies should be required to justify use of that information. This requirement should not be eliminated. If anything, it should be mandatory that insurance companies present their data on their actual losses and experiences in Texas to the insurance commissioner.

OTHER
OPPONENTS
SAY:

There is no definition in the Texas Insurance Code for insurance advisory organizations other than the list of functions performed by these organizations in Art. 5.73 of the Texas Insurance Code. There are similar advisory organizations that offer to insurance companies such services as credit scoring (evaluating credit reports to determine insurance risk) and catastrophe modeling (simulations to determine the potential cost of major disasters). They are not governed by the insurance advisory organization law because these functions are listed in the code. The list of functions should be expanded so that these organizations and their information products can be monitored by the insurance commissioner.

The \$100 license fee is too low compared to other insurance licensing fees, which can be as high as \$2,000 for the first year alone.